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TAGS: [ECON](#) [PGOV](#) [PREL](#) [FM](#) [CH](#)  
SUBJECT: (S) MOBIL REJECTS FSM PETROLEUM CORPORATION PROPOSAL FOR  
FINANCING FROM CHINA

CLASSIFIED BY: Miriam K. Hughes, Ambassador, Amembassy Kolonia,  
State.  
REASON: 1.4 (b), (d)

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[¶1.](#) (S) Summary. In a veil of secrecy, a nascent national petroleum corporation for the Federated States of Micronesia (FSM) has begun to purchase fuel storage tanks from Mobil in all four FSM states. Purchase of the fuel terminals should be complete by the end of July. The President of Mobil in Guam helped broker an FSM loan for USD 9.7 million from the Bank of Guam to ensure direct Guam-based payment to Mobil. Mobil's President said he rejected a proposal by the FSM to cover purchase of the tanks and residual fuel by means of a USD 20 million concession loan from China. As the FSM begins to establish a headquarters for "PetroCorp" on the capital island of Pohnpei in order to purchase fuel in bulk for the entire nation, Mobil believes representatives of the new corporation may return to China to seek a loan to cover costs of future oil supplies and/or interest payments on the loan from the Bank of Guam. End Summary.

#### SECURITY CLOAKS PURCHASE OF FUEL TANKS

[¶2.](#) (C) A national petroleum corporation for the Federated States of Micronesia (FSM) was established by the FSM Congress and signed into law by President Emanuel Mori in September 2007. Since that time, the nascent corporation, which will do business under the trade name of "PetroCorp or FSMPC," has struggled to incorporate all four FSM states. Replacing 42 years of Mobil Oil Micronesia service, FSMPC will acquire and operate fuel storage and wholesale distribution facilities in Yap, Chuuk, Kosrae and Pohnpei States. During the past year, Mobil-Guam has worked fitfully with the FSM national and state governments to try to finalize asset sales and supply agreements. Mobil President and Guam Country Director Kamal Singh (Fijian national) described negotiations as the toughest wrangling he has ever experienced in an 18-year career with Mobil in the Asia and Pacific region.

[¶3.](#) (SBU) Without notification to the public, a transfer of state assets to PetroCorp began in Yap last month. Chuuk then supposedly turned over its assets to FSMPC on July 11. A Mobil media release in Guam on June 28 anticipated that "a full transition of Mobil's assets and operations in FSM to the FSMPC will be completed by the end of July 2008."

[¶4.](#) (SBU) In the absence of public information, speculation on the Internet chat site Micronesian Seminar has run rife. For example, one anonymous commentator wrote: "China and FSM can co-finance gigantic fuel storage tanks in the FSM to assist

refueling of China's submarine fleet program. With larger bulk fuel purchase, the price of fuel will drop in the FSM. FSM's economy can skyrocket within a short duration, probably as fast as China's rate of economic growth." Other commentaries lambaste the silence of the FSM National Government on the current transactions and cast doubt on the dependability and credibility of PetroCorp. The ability to leverage purchasing power from the higher economy of scale derived from national versus state purchases is likely to be undercut by the rising cost of petroleum products, according to industry experts, possibly exacting a political price for the FSM National Government.

#### DEALS FRAUGHT WITH DELAYS - CHINA OFFERS ATTRACTIVE TERMS

15. (C) Since the establishing legislation passed in September 2007, an anticipated USD 9.74 million loan from the Bank of Guam to acquire fuel storage and delivery assets was delayed pending a decision in Pohnpei State about whether to join FSMPC. As a newly elected government in Pohnpei took its time to assess alternative supply options, Mobil threatened to withdraw from the deal. Pohnpei only consented to come on board in March 2008 after President Mori, under intense pressure from Mobil, agreed to sign an indemnification agreement for Pohnpei State operations. In turn, the FSM National Government received a back-to-back indemnification from FSMPC, even though the Corporation still lacks insurance coverage. When Ambassador Hughes asked Pohnpei Governor John Ehsa how the FSM National Government could conceivably cover fuel eventualities in his state, the Governor responded, "That's President Mori's problem." According to Singh, the indemnification agreements are "pure paper."

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16. (C) With Pohnpei on board, the FSM National Government announced that the Bank of Guam would finance the purchase of Mobil assets and FSMPC would commence operations in May. However, FSMPC continues to lack a Chief Executive Officer, technical managers and staff. In the absence of FSMPC managers, negotiations continued under the direction of PetroCorp's Interim Task Force Chief, Secretary of Resources and Development Peter Christian.

17. (S) Singh has shared his understanding that Christian made secret trips to Beijing to secure a loan offer of USD 20 million at a rate of 2 per cent interest. Singh promised to deliver a copy of the draft Chinese loan proposal to Ambassador during his next trip to Kolonia. When Secretary Christian urged Mobil to accept payment through Chinese financing, Singh said he refused, fearing unreliability. Instead, Mobil insisted upon and helped finalize the USD 9.74 million loan from the Bank of Guam. As fuel storage assets are transferred, Mobil-Guam has begun to receive payment directly from the Bank of Guam.

#### FRAGILE FINANCING PORTENDS PETRO-CORP DIFFICULTIES

18. (S) Owing to low revenue generation in the FSM, along with soaring costs of petroleum, foods and basic products in this remote island nation, Singh speculated that Secretary Christian would be tempted to again travel alone to Beijing to seek Chinese financing, either to help defray the cost of fuel supplies or to cover interest payments to the Bank of Guam, which has pegged its loan to FSMPC at 7.5 percent. (Christian alleged to Ambassador that he had succeeded in securing an earlier offer of a 6.5 percent interest rate.) Terms of establishment of the FSMPC, which is a quasi-governmental corporation, circumvent essential FSM Congressional oversight, according to Singh.

19. (SBU) In its efforts to ensure "a seamless changeover" and "product supply continuity," Mobil-Guam's media release states that Mobil remains committed to an ongoing, phased transfer of assets in a nation that it has supplied since 1966. Mobil will remain the sole supplier of FSM fuel for the next five years, including the sale of gasoline, diesel and jet fuel at market

rates, which FSMPC will distribute to the four states. However, Mobil does not disembark tankers from Singapore to the FSM until pre-payment is received. During the first year of transition, Mobil employees in the FSM, including experienced technicians, have supposedly agreed to remain in place at their current salary rates. A petroleum expert from the Pacific Island Forum, who has contributed constant advice, maintains that FSMPC can succeed, particularly if the corporation puts out a tender for future maintenance and delivery services. In the long run, Pacific island nations may be able to negotiate a competitive bulk price, he said. Continental Airlines' regional operational manager commented that Continental will continue to load jet fuel under the FSM's new arrangement, so long as scrupulous quality assurance checks meet security standards at the time of tanking any of its flights. Otherwise, Continental will be compelled to cancel operations.

¶10. (S) Comment: Timing of such a complex transition to a national fuel corporation is clearly complicated by soaring oil costs. At the same time, tensions among the four FSM states and the national government are also running high owing in part to inefficiencies in implementation of declining Compact assistance and perceived favoritism toward President Mori's home state of Chuuk. If FSMPC appears to favor any one of the four states in the supply of oil inconsistent with state payments, dissension will deepen. Political pitfalls for Secretary Christian (Pohnpei State) are clear if his hand is revealed in possible covert loans. In the meantime, many of the fuel tanks in the FSM are deteriorating and they require costly repairs; Mobil was reluctant to invest in their overhaul owing to the paucity of market profit from the FSM. Beijing has supposedly expressed interest in building all new storage facilities. To maintain quality assurance standards and purchase sufficient fuel to avoid blackouts, the FSM will require additional sources of financing. Some observers believe Secretary Christian, who may harbor Presidential ambition, will take credit for launching PetroCorp, and then blame a collapse on FSMPC Board members. Former FSM Vice President Redley Killion is already a member of the board, a contender for Governor of Chuuk and a possible target of blame by Christian.

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